

DIRECTOR OF CENTRAL INTELLIGENCE

Security Committee

SECOM-D-270

4 August 1982

OS REGISTRY
FILE *1104-1*

MEMORANDUM FOR: DCI Security Committee Members and Observers

FROM: Robert E. Leidenheimer
Chairman

SUBJECT: Foreign Ownership, Control or Influence of US Firms

1. There will be an informal meeting of interested SECOM members at 10:00 a.m., Wednesday, 11 August 1982, in room 7D32, CIA Headquarters, to discuss how Community organizations handle security implications of foreign ownership, control or influence of US firms which hold or bid on contracts with the Community. We will explore the possibility of reaching consensus on a uniform, current approach.

2. Attached for information are copies of:

a. The current Community policy on this subject. (This was incorporated in the revision of DCID 1/19 approved by SECOM and the DCI this spring. That revision is being prepared for printing now.)

b. An article on this subject by the Director, Defense Investigative Service.



25X1

Attachments

OS REGISTRY
2-1960

21 APR 1981

MEMORANDUM FOR NATIONAL FOREIGN INTELLIGENCE BOARD

SUBJECT: Policy Concerning Control of Sensitive Compartmented Information (SCI) Released to Contractors or Consultants and to Companies Under Foreign Ownership/Dominance


1. This memorandum establishes policy for releasing SCI to contractors or consultants which may be subject to foreign ownership, control or influence.

Contractor companies under foreign ownership, control or influence will generally be ineligible for access to SCI activities and information. Foreign ownership, control or influence in this instance means that foreign interests own five percent or more of a contractor's voting stock, or they are able through lesser holdings to control or influence the appointment and tenure of the contractor's managing officials. The responsible SIO may waive this provision, however, if a review of the circumstances determines that the following conditions apply: the foreign ownership, control or influence does not involve Communist countries or countries otherwise inimical to the United States, and the foreign interests do not have the right to control or influence the appointment or tenure of a contractor's managing officials. Before a waiver is granted, provision must be made to ensure that security safeguards exist to prevent disclosure of SCI-controlled information to any non-U.S. owners and managing officials. Should foreign ownership increase beyond five percent during the course of a contract, a review of the contractor's eligibility for continued access will be made by the responsible SIO.

2. This policy shall be incorporated as written into DCID 1/19 when it is revised.

/s/ B. R. Inman

B. R. INMAN
Admiral, U. S. Navy
Acting Chairman



Pentagon Corner

BY THOMAS J. O'BRIEN
Director
Defense Investigative Service

Foreign Investment in US Industry

During the 1970s, United States industry experienced an avalanche of foreign investment brought about by world economic conditions. Concern over the national security implications of this unprecedented trend in foreign investment produced a flurry of activity in the Congress and the executive branch.

The Foreign Investment Study Act of 1974 directed the secretaries of commerce and treasury to conduct a comprehensive study of foreign direct and portfolio investment in the US. The cabinet-level Committee on Foreign Investment in the United States was formed to review major foreign investments and assess trends and developments. Numerous bills dealing with regulation and monitoring of foreign investment were introduced in the Congress, and hearings on this topic were held by Congressional committees.

The Department of Defense (DoD) has long recognized that foreign investment in US industry is a cause for special concern where performance on classified contracts is involved. We have a comprehensive policy governing foreign ownership, control, or influence. Although this policy has been fine-tuned to keep abreast of current developments, it has remained essentially unchanged since its inception in 1950. Numerous reviews over the past several years indicate the policy is sound and well able to safeguard our national interests in an economic atmosphere that induces foreign investment.

The DoD policy is of major importance because it governs not only all contractors involved in classified procurement for the Department of Defense, but also those contractors involved in classified procurement for seventeen other departments and agencies of the government. DoD has this responsibility because, under authority of Executive Order 10865,

DoD has entered into agreements with most departments and agencies of the executive branch of the government to administer industrial security on their behalf.

Under this program, a general rule was established that a facility may be cleared only if it is organized and exists under the laws of one of the fifty states or Puerto Rico. Facilities determined to be under foreign ownership, control, or influence are not eligible for a facility security clearance.

Why have this foreign ownership policy? The reason is simple. The Defense Industrial Security Program (DIS) is based on a security agreement that requires classified information to be handled and safeguarded in a prescribed way. That agreement is between the government and the top management of the company involved. If top management is under the control or influence of a foreign interest, it would not be reasonable to entrust a company with classified information that cannot be released to that foreign interest. As a minimum, it would establish an untenable conflict of interest. As a maximum, it would be entrusting classified information to those whom US national policy has dictated should not have it—the foreign government itself.

Whenever significant evidence of foreign ownership, control, or influence is present, the case is discussed in detail with the contractor and his counsel. If it appears an adverse decision is indicated, the contractor is informed, and advice and guidance are provided as to actions the contractor might take to isolate or nullify this foreign ownership. When there is a significant degree of foreign ownership, a voting trust or proxy agreement is sometimes suggested as a means of isolating this foreign owner. The trust can be used to transfer legal title from a foreign owner to trustees who are US citizens. The foreign

owner then becomes simply a beneficiary, but under the proxy agreement retains legal title to the stock. In all other respects, the proxy agreement provides the same isolation as the voting trust. In order for such an arrangement to be approved, the foreign owner must agree to relinquish all the normal prerogatives of management. The trust must be *de facto* as well as *de jure*. In other words, the US trustees must assume responsibility for management and control of the corporation, thereby isolating the foreign owner from the cleared US facility. If there are interlocking directors, the interlocking directors must resign, because otherwise they would tend to circumvent the trust agreement. When a contractor establishes such a trust, it is generally possible for DIS to issue or continue the facility security clearance.

The difficulty frequently encountered in establishing a trust is the reluctance of the foreign investor to relinquish totally the normal prerogatives of management. Unless the foreigner is willing to give up control of his US investment, the trust will not achieve the necessary isolation and the facility clearance cannot be continued.

Trust or proxy agreements have been established only for a very few cleared facilities. More typically, companies have elected not to enter the classified procurement field because their foreign owners have chosen not to relinquish the prerogatives of management.

Some Wall Street analysts believe foreign investment in the United States is now in a downward trend. Nevertheless, our experience of the 1970s indicates that foreign ownership, control, or influence of US cleared defense contractors will continue to be a matter of high priority in both the executive and the legislative branches of the government.

SECURITY MANAGEMENT

MAY 1982

The Director
Central Intelligence Agency



Washington, D.C. 20505

Honorable John W. Warner
United States Senate
Washington, D.C. 20510

Dear Senator Warner:

Thank you very much for your letter of 28 July 1982, expressing your concern regarding the Department of Energy plan to staff the Forrestal Message Center with contractor employees.

It is my understanding that DOE has undertaken this action in compliance with OMB Circular A-76, which encourages the use of contractor personnel instead of Federal employees as an economy measure. The DCI Security Committee is looking into this matter. I have been told that the communications center in question handles classified and compartmented information originated by several other agencies.

While the contractor communicators will have to meet US Government standards of security, including DCI standards for access to sensitive compartmented information, there is some concern in the Intelligence Community that communications functions are so vital and basic to security that they should be entrusted only to Federal employees. Another concern is that material restricted from contractor access, such as industrial proprietary information, should not be exposed to employees of a contractor which might gain an advantage therefrom.

Security elements of the Agency and the Intelligence Community have been aware of this situation for several weeks. When the Security Committee's review of the matter is completed, I will review its recommendations. Please be assured that your concerns will be taken into consideration.

Sincerely,

John N. McMahon
Acting Director of Central Intelligence

DDA 82-1885/6

8 AUG 1982

MEMORANDUM FOR: Director, Office of External Affairs

FROM: Harry E. Fitzwater
Deputy Director for Administration

SUBJECT: Response to Senators Nunn, Goldwater, and Warner
Regarding the Forrestal Message Center

1. It is suggested that our replies for DCI/DDCI signatures to Senators Nunn, Goldwater, and Warner concerning the use of contract personnel at the Forrestal Message Center be formulated as follows:

Thank you for your letter of _____ 1982, expressing your concern regarding the Department of Energy proposal to staff the Forrestal Message Center with contractor employees. I am also very much concerned about the possible impact to the security of classified intelligence-related information if this proposal is adopted. My initial reaction is that the protection of intelligence sources and methods mandates that the responsibility for handling classified communications functions must be maintained in accordance with the security standards currently adhered to by Federal employees.

Security elements of the Agency and the Intelligence Community have been aware of this proposal for several weeks. The Intelligence Community Security Committee is presently conducting a thorough review of this matter and will provide me with its recommendations. Please be assured that your concerns will be taken into consideration.

2. Please advise if there is any additional information that you need in preparing responses on this subject.

ILLEGIB

Harry E. Fitzwater

cc: D/OC
D/ODP
D/OS

